

**What is the World Bank Good For?
Global Public Goods and Global Institutions***

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Abstract

The World Bank is in the doldrums, or worse. The Global Public Goods (GPGs) argument is often put forward as a way of reviving and even rescuing an institution whose financial base to support conventional sovereign loans is receding sharply relative to needs and competition from other sources. The World Bank does have certain advantages as an institution, which the global community could use to address GPG issues. It has technical excellence and convening power to help build consensus on a range of GPG issues, although this cannot be fully realized without radical reform of its governance structures. It has experience with managing concessional and grant resources, which will be central to financing GPG mechanisms. And it also has experience with country operations to implement the country specific dimensions of GPG mechanisms. That is what the World Bank is good for now, three quarters of a century after its founding.

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1. Introduction

It should be clear to even a casual observer that all is not well with the World Bank. Staff morale is low. Discourse on “Mission creep” co-exists with “Lack of Mission”. Shareholders do not seem to be in love with the institution either. Using the indicator of the (lack of) success of the last capital increase, compared to the relative success of the Regional Development Banks and the IMF, and the propensity of subsets of shareholders to set up new multilateral development banks (MDBs), the shareholders of the World Bank do not seem to be putting their money where their mouths are, even when they mouth support for the institution.

But this was not always so. The World Bank was a prized institution, credited with its share of glory for the post second world war recovery. Even when it was criticized and reviled by civil society in the years of structural adjustment and the Washington consensus, at least it demonstrated its relevance. The risk now is growing irrelevance as its financial base recedes relative to financial needs of countries on the one hand, and alternative supplies of finance on the other.

So much for the World Bank. Coming to the World itself, there is now a growing understanding, to the point of a crescendo of recognition, of the problems of cross-border spillovers and externalities, and of the inadequacy of instruments to address these problems. Obviously, the problems include financial contagion, infectious diseases, climate change and migration. Our Westphalian world of nation states is struggling to address these problems, for the equally obvious reason that there are insufficient incentives for any single country to invest in the solution, which must necessarily be cross-national.

We thus have a global institution which is falling into difficulties and irrelevance; and a set of problems which need a global institution to address them. Could there be a match? And what would need to happen for the match to be made and for it to succeed? These are the questions which I try to begin answering in this presentation. Although I will put forward general frameworks, my motivating focus is on a single institution, The World Bank, and its potential role in addressing the problem of Global Public Goods.

2. The Bretton Woods Roots of the World Bank and its Instruments

The International Bank for Reconstruction and Development (IBRD) emerged out of the Bretton Woods conference of 1944 as an institution designed by John Maynard Keynes and Harry Dexter White to help intermediate between the availability of finance in the US, and the need for it in a bombed out Europe and Japan. The emotional and moral roots of the institution were presaged by Keynes a quarter of a century earlier in his *Economic Consequences of the Peace*:

“...the spokesmen of the French and British peoples have run the risk of completing the ruin which Germany began, by a peace which, if it is carried into effect, must impair yet further, when it might have restored, the delicate, complicated organization, already shaken and broken by war, through which European peoples can employ themselves and live.....If the European war is to end with France and Italy abusing their momentary victorious power to destroy Germany and Austria-Hungary now prostrate, they invite their own destruction also...” (Keynes, 1919, pp 1-2)

The sovereign loan instrument which is the hallmark of World Bank operations was designed to address the market’s reluctance to invest in infrastructure in these countries on a normal commercial basis. It was the brainchild of Keynes, who was the chair of “Commission II” at Bretton Woods, on “The Bank for Reconstruction and Development.”¹ In his opening remarks to the first meeting of the Commission on 3 July, 1944, Keynes set out the objectives of the Bank as follows:

“...it will be authorised in proper cases and with due prudence to make loans to the countries of the world which have suffered from devastation of war, to enable them to restore their shattered economies and replace the instruments of production which have been lost or destroyed.....[A]s soon as possible, and with increasing emphasis as time goes on, there is a second primary duty laid upon it, to develop the resources and productive capacity of the world, with special attention to the less developed countries....” (Keynes, 1944, pp 72-23)

To meet these objectives, Keynes proposed a specific type of loan guarantee to overcome the inherent risks of lending to war torn countries:

“Only those countries which find themselves in especially favoured positions can provide the loanable funds. But this is no reason why these lending countries should also run the whole risk of the transaction. In the dangerous and precarious days which lie ahead, the risk of the lender will be inevitably large and most difficult to calculate. The risk premium reckoned on strict commercial principles may be beyond the capacity of an impoverished borrower to meet, and may itself contribute to risks of ultimate default.....The proposal is, therefore, that all the member countries should share the risk in proportions which correspond to their capacity. The guarantees will be joint and several, up to the limit of any members’ subscription, so that the failure of any member to implement his guarantee will not injuriously affect the lender..... I fancy that the underlying conception of a joint and several guarantee of all the member countries throughout the world, in virtue of which they share the risks of projects of common interest and advantage even when they cannot themselves provide the lump sum loan originally required, thus separating the carrying of risk from the provision of funds, may be a contribution of fundamental value and importance to those difficult, those almost overwhelming tasks

¹ Commission I, on the IMF, was chaired by the Keynes’s American counterpart Harry Dexter White.

which lie ahead of us, to rebuild the world when a final victory over the forces of evil opens the way to a new age of peace and progress after great afflictions.” (Keynes, 1944, pp 74-75).

The contribution of the International Bank for Reconstruction and Development to the dramatic post war recovery is a testament to the success of the Keynesian design of sovereign lending. As the remarkable growth of Europe and Japan in the next quarter century reduced this need, and as Keynes had asked in that very first meeting of Commission II, the institution turned to developing countries, further bolstering its resources with the concessional loan window of the International Development Association (IDA). The model was also replicated through the Regional Development Banks and sub-Regional Development Banks. The reasons for this proliferation of the model, which continues to this day through AIIB and NDB, are perhaps mainly political, but the proliferation is testament to the power of the sovereign loan model itself.

For the second next quarter century after Bretton Woods, the World Bank of IBRD and IDA was the biggest game in town for most developing countries and in some cases the only game in town. As the institution approached its half century, the protest movement “Fifty Years is Enough” signified disenchantment with the World Bank (and of course its Bretton Woods twin, the IMF) but, equally, it signified the relevance and importance of the institution for development. It is this relevance which is at issue now, having crept up on us as we approach seventy five years of the World Bank in 2019, and as we look beyond that to the next quarter century of the institution.

The international development assistance landscape is now very different from that at the time of Bretton Woods, and even from that which pertained fifty years after 1944. The World Bank is now decidedly not the only game in town in providing development finance. In the official sphere, multilateral development banks (MDBs) emerged to provide regional counterbalance. Regional Development Banks were founded from the late 1950s onwards, supplemented by sub-regional entities. In the last decade, the World Bank received relatively meagre capital increases compared to these regional and sub-regional entities. Other MDBs like the Islamic Development Bank also began operation and have grown. Most recently, the Asian Infrastructure Investment Bank (AIIB) led by China was launched in 2014, and the New Development Bank (NDB) was launched by Brazil, Russia, India, China and South Africa (the BRICS countries) in 2015.

A common narrative for the emergence of these alternative sources of development finance is that they have emerged in response to the perceived US and European dominance in the governance of the World Bank. But whatever the reason, the vast bulk of development resources now lie outside of the World Bank. This is even more the case if we include the burgeoning of bilateral programs, and non-private sector non-governmental funding like that from the Gates Foundation. And of course private sector flows have increase beyond all recognition in the last quarter century.

The vast expansion of institutions and official sources of finance outside of the World Bank must surely mean that over the next quarter century the resources that the World Bank can devote to its signature country specific development activities are bound to diminish drastically relative to development needs. Indeed this unmet need for infrastructure investment, which it is argued traditional sources could not meet, has been a principal rationale advanced for the NDB and AIIB. Of course, the capital that went into these new institutions could have gone into the World Bank, but it did not. As noted earlier there is a political reason for this. But there is also an operational rationale, based on the efficacy of having institutions close to their operations.

But notice that in the original conception of Keynes, the use of funds is basically for country level investment. There is no mention of the modern cross-border issues of climate change, infectious disease control, migration, or financial contagion as being part of the remit of the World Bank. These are of course the issues of our time. But, in keeping with the original model, despite a ramping up of rhetoric from all multilateral development banks on cross-border spillover and public goods, the overwhelming focus is still on country by country investment.

What, then, is the World Bank good for in the next quarter century? What role would John Maynard Keynes and Harry Dexter White assign to a global development institution in a world in which there already was a plethora of institutions addressing flows of funds to individual countries for investment? The answer has to be: issues which are truly global in scope, issues which cut not just across countries but across regions of the world as well. It is these issues which cannot be satisfactorily addressed by the proliferation of regional institutions, nor indeed by non-governmental institutions, nor of course by private capital flows. In other words, Global Public Goods. But what does the theory of global public goods (GPGs) tell us about the division of labor in their supply?

3. Global Public Goods: Theory and Division of Labor

To begin at the beginning, a public good in economics text books is one that is “non-rival” and “non-excludable.” By non-rival is meant that consumption by one party does not reduce the amount available for others’ consumption. A beautiful sunset is non-rival. An apple is not. By non-excludable is meant that no one in a defined group can be or is excluded from consumption. An open public beach is non-excludable. A fenced off private beach is not.

But there are of course many points of nuance. A “pure” public good is one which is fully non-rival and non-excludable. Partial or incomplete fulfilment of these requirements leads to intermediate cases, which are typical. Further, the properties of non-rivalry or non-excludability may be inherent and technological, for example the rivalry of apple consumption. But they can also be, and often are, features of human design. For example, NATO’s fundamental principle “an attack on one is an attack on all” introduces non-rivalry and non-excludability as an institutional design feature. Externalities, spillovers across parties not appropriately mediated through markets, are closely related to public goods but are not the same. A mechanism to address an externality is a public good to the extent that the mechanism is non-rival and non-excludable. And when a public good mechanism is in place the mechanism has to take into account the externalities caused by free riding.

There are many externalities and spillovers across sovereign nation states. Four obvious ones mentioned earlier are financial contagion, infectious diseases, climate change and migration. But another important aspect of these spillovers is their reach and spread. Many are restricted to a contained number of contiguous nation states. For example, riparian rights across countries sharing river basins and water tables, or when forest cover or wildlife movements stretch across borders, or when conflict in one country leads to refugee flows only to a neighboring country.

There are conflicting tradeoffs in designing mechanisms and institutions to address these cross-border externalities. And it is these mechanisms and institutions which are the public goods. The principle of subsidiarity says that all other things equal, and if the setting up of mechanisms were costless, the mechanism addressing a problem should be located closest to where that problem is. Thus the principle would resist an immediate jump to a global institution to address multi-country issues in Africa, or in Latin America, or in Asia.

Of course, mechanisms and institutions are not costless. There are large fixed costs of setting up institutions, which suggests a small number of institutions. But how many and of what type? A detailed cost-benefit would be difficult if not impossible to conduct, but suggests a split between Regional Institutions for within-region spillovers and Global Institutions for spillovers which are global in the sense that they encompass countries from across regions. There is no reason why a three-country riparian rights issue in Asia, for example, should necessarily be handled by a global institution like the World Bank if there is a regional institution capable of handling it. If the subsidiarity argument has validity, then Regional Public Goods (RPGs) should be handled by Regional Institutions, and GPGs by Global Institutions. Thus for a Global Institution like the World Bank, the rationale for involvement in cross-border externalities cannot simply be that they exist, but that they are Global and cross-regional in nature.

There is yet another type of question on the division of labor. For truly global issues, should there be a global institution per issue, or should there be a global institution handling multiple issues? There is a

tension or tradeoff between issue focus and design of the mechanism at the global level (which is the GPG), for example for infectious diseases, and implementation of the mechanism at the country level. A smooth translation from one to the other is necessary, and this may be best achieved by having both under one roof, but the trade off has to be recognized.²

Notice that addressing the consequences of the lack of a GPG is not the same as provision of the GPG. Thus support for mitigation efforts on climate change is support for a GPG. But support for adaptation to climate change, for example adapting infrastructure to sea level rises, is not. This latter is on par with support for other dimensions of addressing the conditions of lack of development, like low levels of education or health.

This brings us to a fundamental point about the trade offs in use of resources of the development banks, the World Bank in particular. Should they be used for development and poverty reduction on a country by country basis, or should they be used for provision of GPGs? Of course one could avoid the question by saying that GPGs address development and poverty reduction as well. But this does not face up to the tradeoff that the marginal dollar could be spent on building schools or health posts versus developing clean energy devices to reduce fossil fuel usage.

This is not an easy question to answer definitively and quantitatively. But it can be argued that up to now resources of the development banks have only been minimally devoted to GPGs. There should be a shift towards (i) financing the setting up of global mechanisms to address GPGs and (ii) financing the country specific investments required by the global mechanism. However, Ray Offenheiser provides an alternative perspective in a dissenting note to the recent Center for Global Development report on Multilateral Development Banks:

“What separates the MDBs in this fast-changing context, however, is their specific mandate to reduce poverty....While I would certainly recognize the role of global public goods (GPGs) in addressing different dimensions of poverty and inequality...and perhaps even recommend making it an explicit and major pillar of work, I would continue to argue that the overarching mission and mandate of the World Bank (and other MDBs) must remain the fight to eliminate extreme poverty.” (Center for Global Development, 2016, p 27)

This is surely a different voice on the division of labor between financing for GPGs and financing for country specific investments for poverty reduction.

However, the financing issue immediately brings up another fundamental question—the suitability of the development banks’ signature instrument, the sovereign loan, for financing GPG mechanisms. The host of truly global cross-border issues which face our globalized world require a global response. Yet the implementation of these responses, for climate change, financial contagion, infectious diseases and migration, will have to be at the country level in a world which is still Westphalian in its structure and likely to remain so into the foreseeable future. We thus need responses which will entail specific concentrated short term costs on some countries with the promise of more diffuse long term gains for all. This is a classic coordination problem for which the World Bank’s standard

² Of course there is a further requirement if the World Bank, or any other development bank, is to involve itself in GPGs—there has to be a strong and direct development impact of the creation and maintenance of the GPG. A global yacht club for the super rich is a GPG of sorts, but hardly something a development bank should put resources into!

instrument, the sovereign loan, is highly unsuited. Loans, and their repayment, require specification of who receives the loan and who repays, while the nature of the problem is that the benefits of addressing cross-border issues, while they may be large in aggregate, cannot be attributed quite so easily to individual parties. Of course various methods such as apex loans to joint entities, can be and have been tried. But they cannot fully overcome the basic design problem.³

For these reasons, a grant instrument is more suitable than the World Bank's classic sovereign loan, which proved so successful in addressing the problems of 1944. This is recognized in a recent Center for Global Development (2016) Report which proposes a new grant financing window for the World Bank alone of \$10b annually. It raises the question then of whether similar windows should also be opened for the regional development banks. And it is the use of grant resources in this manner, rather than for direct poverty reduction, which Ray Offenheiser is dissenting from.

³ It is indeed a high irony that the "joint and several" guarantee is itself a public good for the shareholders of the World Bank, with its elements of non-rivalry and non-excludability.

4. World Bank Specifics

So, what is the World Bank good for? As an institution for country specific investment for development and poverty reduction, the world community has revealed a preference for other institutions—regional development banks, new development banks, and other multilateral and bilateral vehicles. It is not clear if this trend can be reversed. Ironically, the core instrument of these institutions is the sovereign loan with “joint and several guarantee” so brilliantly conceptualized and devised by Keynes. The proliferation of institutions with the same structure and core instrument is a tribute to Keynes, but it is cold comfort to the World Bank whose financial weight and influence diminish every year as the developing world grows.

There appears to be more global support for a generic GPG argument for development financing. For example, the \$100 billion dollars a year pledged for Climate Change at the Paris Conference of Parties in 2015, for all its softness in terms of likely actual outcomes, is an indication at least of global aspirations. Other initiatives which pool donor funds for cross-country activities are also an encouraging indicator. But there are strong caveats to be made before we jump from this to the World Bank as the institution to implement these initiatives:

- For region specific cross-country public goods, regional institutions are superior in principle.
- For genuinely global GPGs, there is the question of whether the world community should primarily go for issue specific global institutions.
- The sovereign loan instrument is not suitable for GPGs, and there are significant tradeoffs in use of grant resources for GPGs rather than country specific poverty reduction.

Nevertheless, however, there are strong arguments for the international community using the World Bank to advance the GPG agenda:

- It is indeed a global institution, with a global mandate and, although as yet inadequate, a potentially reformable governance structure.
- Its country specific operations give it a platform to implement the country level actions needed in a global mechanism.
- It has experience of, and is trusted in, managing concessional funding, and trust fund grant funding.

If the international community wished to, it could build on these strengths and develop a GPG mandate for the World Bank, as argued in the Center for Global Development (2016) Report, which recommended a grant facility of \$100 billion per year for this purpose.

The basic problem with achieving this vision of the World Bank as the world’s premier global (not regional) public goods agency is precisely that it still reflects the assumptions and the structures that were appropriate for 75 years ago. Its staff are suited to country specific operations, and its lead instrument is lending. Its country specific lending operations need to be shifted, gradually but purposively, to regional and sub-regional development banks. This shift would of course not be immediate, and would move at different pace in different regions. In Latin America or Asia the move could be much faster than in Africa. But shift it must. The subsidiarity principle demands no less.

At the same time, the institution needs to transform itself from a lending institution to one which operates through a grant modality. Its existing reserves could be put to generating income for

grant outlays as opposed to shaving points off the interest rates on its loans. Further, staff expertise will need to be built up not only on the key sectors which need global public goods, but in developing and maintaining multi country grant operations. The composition of staff will therefore change. As to the level of staffing this depends on who well the institution dies from the perspectives of shareholders. There is no necessary reason why it should shrink in size—GPG issues are surely large enough to warrant the current staff strength if not more.

Beyond the standard GPGs there is, in particular, one GPG for which the international community already relies on the World Bank, and which the World Bank could do more of. GPGs are contentious issues and it is not easy to arrive at a global consensus on the way forward, in general and in specifics. And without a consensus there is no way forward—that is almost definitional for a GPG, which requires multi-country action. But the development of global consensus is itself a GPG. It is surely global, and a consensus is non-rival and non-excludable. Thus consensus on GPGs has all the issues of underinvestment faced by other GPGs. No single party has the full incentive to achieve consensus, because the costs are party specific but the benefits are dispersed.

The international community needs institutions which help to develop global consensus, and to maintain it. The role of globally acceptable data and analysis is crucial. For example, SDG 1.1 is to eliminate extreme poverty. But who is to define extreme poverty? Who is to collect, collate and manage the data to monitor this global goal? Who is to develop and maintain global consensus on these seemingly technical but often starkly political questions? The recent report of the Atkinson Commission on measurement of global poverty, commissioned by the World Bank, is an example of a consensus building exercise which can help the global community come together around SDG 1.1 and other SDGs (Commission on Global Poverty, 2016). It is a significant contribution to an underappreciated GPG.

Consensus building of this type has two prerequisites—technical excellence and actual and perceived independence. Both of these were satisfied in the case of the Atkinson Commission. But the governance structure of the World Bank mitigates against perceived and perhaps actual independence of consensus building exercises. These structures have to move to reflect the economic realities of mid 21st century, rather than the realities of the mid-20th century. All GPGs require multi-country consensus, and this consensus will not be easily arrived at by an institution whose governance structures are set in 1944 rather than 2019. If a new Bretton Woods conference were to be held today, it would be unlikely that it would be dominated by just two names—Keynes and White—simply because the economic weights of other countries are now much more significant. For the same reason, an institution which purports to address cross-border issues which span the globe will need adequate representation from across the globe reflecting economic and political weights of our time.

But the reality of the current capital increase impasse at the World Bank is also clear. The US is unwilling to put significantly more money of its own towards a capital increase. But it is also unwilling for others to put more money in, lest this dilute its share of capita to below the crucial 15% which gives it a veto. Many European countries in effect take a similar view, unwilling to see a dilution of their voting power and thus unwilling to see a capital increase funded by others, yet unwilling to fund a capital increase themselves. With this impasse, the World Bank will indeed fade into insignificance as global magnitudes pass it by.

The answer to this impasse seems to be a gradual move to a grant making institution where voting power depends on a combination of financial contribution and financial use. Countries which

contribute most, and countries which the world needs to do most to address cross-border global issues, should surely be prominent in the governance of the institution. It is only with this combination that the World Bank can best serve the global needs that only a global institution can do.

5. Conclusion

The World Bank is in the doldrums, or worse. The GPG argument is often put forward as a way of reviving and even rescuing the institution. The argument has merit, but it needs to be unpacked and examined critically. As argued in this paper, first, the GPGs in question have to be genuinely global, not just regional, for a global institution to be given the lead in addressing the issue. Second, there may be an argument for issue-specific global institutions, for example for infectious diseases. Third, the central instrument of the World Bank, the sovereign country loan, is unsuited to financing of GPGs.

However, the World Bank does have certain advantages as an institution which the global community can use to address GPG issues. It has technical excellence and convening power to help build consensus on a range of GPG issues, although this cannot be fully realized without radical reform of its governance structures. It has experience with managing concessional and grant resources which will be central to financing GPGs mechanisms. And it also has experience with country operations to implement the country specific dimensions of GPG mechanisms.

Thus, a combination of (i) continued country specific operations of the conventional type in the short term, but a rapid relative expansion of (ii) focus on consensus building on and design of GPG mechanisms and (iii) their implementation at the country level through grant funding, seems to be the road to viability for the World Bank. That is what the World Bank is good for now, three quarters of a century after its founding.

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